No. 87-1216

IN THE
Supreme Court of the United States
October Term, 1987

ARTHUR YOUNG & COMPANY,
Petitioner,

v.

ROBERT BURULL and JEANNE BURULL,
Respondents.

ON CERTIORARI TO THE UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

BRIEF OF RESPONDENTS IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

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STATEMENT OF THE CASE

The Eighth Circuit opinion, reproduced at pages A-2 through A-5 of the Petition,[1] contains a concise statement of the relevant facts and the proceedings in the district court, 831 F.2d 788 (8th Cir. 1987). The Eighth Circuit opinion is more accurate, dispassionate, and balanced than Petitioner's statement.[2]

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[1] All citations to the record are to the appendix to the Petition.

[2] The misleading nature of Petitioner's statement of the case is reflected in Petitioner's statement that the 10b-5 claim Mr. and Mrs. Burull asserted against Arthur Young was the only claim that permitted the Burulls to escape Arthur Young's two summary judgment motions. Petitioner, at 3. Arthur Young continues this argument by stating that on the third day of trial the Burulls stipulated to withdrawing their primary liability claim under §10(b) of the 1934 Securities Exchange Act and Rule 10b-5 because they had no evidence that Arthur Young had any involvement "with respect to events before July 1983" (*id*).

But dismissal of the primary liability claim left intact Burulls' separate claim that Arthur Young had aided and abetted a 10b-5 violation. Court of Appeals, at A-4, n.6. Moreover, the July 1983 date is of no legal significance, since one can be a member of a conspiracy even though one was not part of the scheme from the beginning. *United States v. Burchinal*, 657 F.2d 985 (8th Cir. 1981). In addition, the withdrawal of a claim does not mean that there is no evidence to support the claim. Furthermore, there is no evidence in the record that supports a finding that this claim was not well grounded in fact and warranted by existing law when this pleading was signed or at the moment of withdrawal or at any other time. As Petitioners have failed to provide a transcript of the proceedings, the record presumptively supports the lower court's decision. *See, e.g., Farrar v. Cain*, 756 F.2d 1148, 1152 (5th Cir. 1985).

Remarkably, Petitioner omits that in addition to surviving two summary judgment motions, Burulls also survived Petitioner's motion for a directed verdict. Even with hindsight, the trial judge was unable to conclude when considering Petitioner's post-trial motions, "that the Burulls' claims were plainly frivolous or without any factual foundation" (Appendix to Petition, at B-11). Common law claims were also submitted to the jury.

REASONS FOR DENYING THE WRIT

Stripped of its verbiage, the petition requests this court to address a very simple question: whether the district court and the court of appeals erred in considering its motions for sanctions under Fed. R. Civ. P. 11 and 28 U.S.C. §1927. The basis of Petitioner's Rule 11 contention is that the final version of the Burulls' complaint contained two counts (in a multiple count pleading) asserted against Arthur Young that were legally deficient. This court denied a similar request for review of denial of sanctions in a case that contained both colorable and non-colorable claims, *Oliveri v. Thompson*, 803 F.2d 1265, 1280 (2d Cir. 1986), *cert. denied sub nom. County of Suffolk v. Graseck*, 107 S.Ct. 1373 (1987), and should also deny this petition.[3] The basis of Petitioner's claim to entitlement to sanctions under 28 U.S.C. §1927 is that the Burulls' case was fueled by Respondent Robert Burull's filing a faulty bankruptcy petition and on the ground of generalized trial misconduct by counsel. The Petition should be denied for the following reasons.

I. THE COMPLAINT DID NOT VIOLATE RULE 11.

Petitioner Arthur Young falsely states "[t]hat rule 11 was violated in this case is not in issue." Petition, at 9. The Court of Appeals found that sanctions "under Rule 11 . . . are . . . mandatory"—and, affirmed the denial of sanctions by the district court. Court of Appeals, at A-5. *See also Thomas v. Capital Security Services, Inc.*, Slip. op., No. 86-4480 (5th Cir. January 21, 1988) (*en banc*) (sanctions under Rule 11

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[3] *County of Suffolk v. Graseck*, 107 S.Ct. 1373 (1987), presented the question to this Court: "Is court of appeals in conflict with all of the other circuits in ignoring the plain language of Fed. R. Civ. P. 11 by fashioning 'de minimus' exception?" *Id.*, at 55 U.S.L.W. 3588 (1987).

mandatory). The district court found only a "technical" violation of Rule 11 (citing *Oliveri v. Thompson*, 803 F.2d 1265, 1280 (2d Cir. 1986), *cert. denied sub nom., County of Suffolk v. Graseck*, 107 S.Ct. 1373 (1987)), which would not support Rule 11 sanctions. Hence, no Rule 11 violation has been found by the lower courts.

A. A Meritorious Complaint That Contains Counts That Are Dismissed Sua Sponte Before Any Response Is Made Does Not Violate Rule 11 Under The Facts Of This Case.

The final version of the complaint contained 23 counts. Included in the counts alleged against Arthur Young were counts stating that Arthur Young acted in violation of §§12 (2) and 17(a) of the Securities Act of 1933 (15 U.S.C. 77(a) et seq.). It is a matter of dispute in the circuit courts of appeal whether §17(a) can be asserted by private litigants. Hazen, THE LAW OF SECURITIES REGULATION §13.13 (1985) ("Most courts that have heard the question have implied a section 17(a) remedy, although there is an increasing body of substantial authority to the contrary [footnote omitted]"). The Eighth Circuit has held that §17(a) provides no private remedy. Section 12(2) applies only to purchasers of securities; Burulls were sellers of securities. These counts were "dismissed by the District Court on its own motion, only a week after plaintiffs filed their pleading. Defendants were never called on to address these claims in any pleading or brief." Court of Appeals, at A-4. Moreover, the offending parts of the pleading were dismissed during the period in which the Burulls had the absolute right to withdraw the pleading. Fed. R. Civ. P. 15(a).

The Court of Appeals in refusing to find a Rule 11 violation held: "Whether meritless elements combine to render the

pleading frivolous as a whole is a 'matter for the court to determine, and this determination involves matters of judgments and degree.' *O'Connell v. Champion International Corp.*, 812 F.2d 393, 395 (8th Cir. 1987)." Court of Appeals, at A-4. Applying this abuse of discretion standard to this case, the Court of Appeals found that the Burulls' §§12(2) and 17(a) claims, "viewed in isolation would be the appropriate subject of a sanction", but the claims when integrated with the rest of the complaint did not so infect the complaint as to render the pleading not well grounded in fact and warranted by law. *Id.* This holding, as shown immediately below, is supported by decisional law. Any other holding would defeat the purpose of Rule 11 by creating satellite litigation in virtually every lawsuit in which there is a "winner" and "loser."

Rule 11 does not mandate that whenever a pleading contains an error that the rule is violated and sanctions must be granted. As stated in *Golden Eagle Distributing Corp. v. Burroughs Corp.*, 801 F.2d 1531, 1540-41 (9th Cir. 1986):

> Moreover, the Rule does not apply to the mere making of a frivolous argument. The Rule permits the imposition of sanctions only when the "pleading, motion, or other paper" itself is frivolous, not when one of the arguments in support of a pleading is frivolous. . . . In short, the fact that the court concluded that one argument or subargument in support of an otherwise valid motion, pleading, or other paper is unmeritorious does not warrant finding that the motion or pleading is frivolous or that the Rule has been violated.

Accord Baden v. Craig-Hallum, Inc., 646 F.Supp. 483, 493 (D. Minn. 1986); *Oliveri v. Thompson*, 803 F.2d 1265, 1280 (2d Cir. 1986), *cert. denied sub nom. County of Suffolk v. Graseck*, 107 S.Ct. 1373; *Rateree v. Rocket*, 630 F.Supp. 763, 778 (N.D. Ill. 1986).

The Third Circuit in *Gaiardo v. Ethyl Corp.*, No. 875248, slip. op. at 10-11, (Dec. 14, 1987) (per Judge Weis) recently applied the *Golden Eagle* analysis:

> As we emphasized in *Morristown Daily Record Inc. v. Graphic Communications Union Local 8N*, No. 875321, slip op. at 2 n.1 (3d Cir. Oct. 29, 1987), when issues are close, the invocation of Rule 11 borders on the abusive: "We caution litigants that Rule 11 is intended for only exceptional circumstances." Nothing in the language of the Rule or the Advisory Committee Notes supports the view that "the Rule empowers the district court to impose sanctions on lawyers simply because a particular argument or ground for relief contained in a nonfrivolous motion is found by the district court to be unjustified." *Golden Eagle Distrib. Corp. v. Burroughs Corp.*, 801 F.2d 1531, 1540-41 (9th Cir. 1986).

The Petitioner has identified no cases that are in conflict with this authority. Petitioner cites *Tedeschi v. Smith Barney, Harris Upham & Co.*, 757 F.2d 465, 466 (2d Cir.), *cert. denied*, 474 U.S. 850 (1985), as in conflict. *Tedeschi* is readily distinguished on its facts, as that case involves a plaintiff and his attorney bringing an action that was revealed to be predominated by frivolous claims in an arbitration hearing. The district court dismissed all five of the plaintiffs' claims before trial, finding that the action was instituted in bad faith without legal or factual support for any of the claims except one, and that claim was barred by the statute of limitations. *Tedeschi v. Smith Barney, Harris Upham & Co., Inc.*, 579 F.Supp. 657, 661 (S.D.N.Y. 1984). This is in contrast to this case where the district court could not find that the "Burulls' claims were plainly frivolous or without factual foundation" (B-11).

Quiros v. Hernandez Colon, 800 F.2d 1, 2-3 (1st Cir. 1986), cited by Petitioner, as in conflict, is not in conflict. *Quiros* affirmed the denial of attorney's fees under 42 U.S.C. §1988 to a prevailing defendant. The Court stated in the context of the Civil Rights Attorney's Fees Act that it was "reluctant to adopt a rule requiring a court to engage in such fine tuning that it must award fees as to an insubstantial claim even though another claim was more substantial and perhaps even prevailed." *Id.* at 2. In *Quiros* the non-prevailing party had fees assessed against him under Rule 11. This award was not appealed. Accordingly, no Rule 11 issue was before the First Circuit.

The Seventh Circuit has developed a line of cases cited by Petitioner that at first appears in conflict with the cases just cited. Petitioner, at 9-10. *See Szabo Food Serv. Inc. v. Canteen Corp.*, 823 F.2d 1073, 1077 (7th Cir. 1987), *petition for cert. filed*, 56 U.S.L.W. 3416 (Nov. 20, 1987) (No. 87-828). These cases are not in conflict as Judge Easterbrook, a moving force behind Rule 11 jurisprudence in the Seventh Circuit, would seemingly confine Rule 11 sanctions to "serious" cases and would not apply the Rule where the motion for sanctions is "foolish." *Szabo*, at 1084.[4]

If the rule were otherwise, every pleading peccadillo would violate Rule 11 and sanctions thereby mandated. The absurdity of this reductionist approach can be revealed by way

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[4] *Szabo* was remanded to determine whether the district court erred in failing to sanction. Judge Cudahy dissented stating this remand "opens new vistas for litigation . . . that will add more to our [appellate] burden than sanctions for 'objectively frivolous' cases will take away. 823 F.2d at 1086.

of an example. A pleading is filed, determined by counsel to be legally and/or factually deficient, is then withdrawn by counsel before receipt by the opposing party. Under Petitioner's scenario, this pleading would be subject to *mandatory* sanctions.

If Petitioner's argument were self-directed, its own answer violates Rule 11 by averring that the Burulls' complaint failed to state a claim upon which relief may be granted. As the Burulls' complaint was sufficient to get to the jury, a *prima facie* case was presented and Petitioner's answer claiming that the Burulls failed to state a claim upon which relief can be granted was neither supported by law nor by the developed facts.

As observed by Professor Nelken, *Sanctions Under Amended Federal Rule 11—Some "Chilling" Problems in the Struggle Between Compensation and Punishment*, 74 GEO. L. J. 1313 1328 (1986):

> The widely assumed right of a defendant to put a plaintiff to his proof is not supported by the Federal Rules. Indeed, Rule 8(b) permits a general denial only "subject to the obligations set forth in Rule 11"; frivolous answers violate rule 11 no less than frivolous complaints. Can a defense lawyer, any more than plaintiff's lawyer, take her clients' word in preparing pleadings?
>
> Similarly, the common practice of reciting a laundry list of affirmative defenses should be closely scrutinized under rule 11. . . . If plaintiffs begin to challenge the factual and legal adequacy of defendants' pleadings under rule 11, the use of sanctions will profoundly affect the "game" of litigation [footnotes omitted].

As the source of Rule 11 is Equity Rule 24, Equity Rules of 1842,[5] and amended Rule 11 builds on equity practice,[6] a Rule 11 movant seeks equity and must be free of unclean hands.[7]

B. Rule 11 Does Not Apply To *De Minimis* Violations.

If Respondents violated Rule 11 in this case by pleading one claim that was not recognized in the Eighth Circuit but is recognized elsewhere[8] and by pleading a count that was legally deficient because the law provides a remedy for purchasers of securities and not sellers, the violation was *de minimis* only and, accordingly, the violation does not support a sanction award under Rule 11.

Where a pleading is in error and that error involves neither significant litigant expense nor significant expenditure of judicial time, sanctions are not warranted, let alone appellate review. In *Oliveri v. Thompson*, 803 F.2d 1265, 1280 (2d Cir. 1986), *cert. denied sub nom. County of Suffolk v. Graseck*, 107 S.Ct. 1373 (1987), Judge Pratt writing for the Second Circuit found that a complaint that contained both claims of merit and deficient claims was in technical violation of Rule 11, but since the infraction was *de minimis* sanctions were not mandated, at least, as here, where the parties have not spent any significant time on the claims. *See also Baden v. Craig-Hallum, Inc.*, 646 F.Supp. 483, 493 (D. Minn. 1986). This is not to say, as suggested in the Petition at 9, that the

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[5] *See* Risinger, Honesty in Pleading and Its Enforcement: Some "Striking" Problems with Federal Rule of Civil Procedure 11, 61 Minn. L. Rev. (1976).

[6] Fed. R. Civ. P. 11 advisory committee's note.

[7] In denying Rule 11 sanctions, Judge Shadur remarked, "defendants' . . . Rule 11 motion may call into play the well-known legal proposition that people who live in glass houses shouldn't throw stones. *Rateree v. Rockett*, 630 F.Supp. 778, n.26 (N.D.Ill. 1986).

[8] *See* Hazen, THE LAW OF SECURITIES REGULATION §13.13 (1985).

mere insertion of a nonfrivolous claim in a pleading, motion, or other paper will permit escape from Rule 11. In the words of the Court of Appeals: "Whether meritless elements of a complaint combine to render the pleading frivolous as a whole is a 'matter for the [district] court to determine, and this determination involves matters of judgments and degree.' [footnote omitted]" (A-4). To entertain sanctions for *de minimis* violations, as Petitioner argues, will demean the litigation process to a far greater extent than do minor, but regrettable, pleading errors that are corrected before the courts or the litigants are put to any untoward effort.[9]

II. SANCTIONS ARE NOT WARRANTED UNDER 28 U.S.C. §1927.

Petitioner seeks sanctions under 28 U.S.C. §1927[10] on the basis of trial misconduct and the filing of a false debtor's petition in bankruptcy court by Robert Burull with the aid of counsel before this litigation began.

A court that finds a violation of §1927 "may" impose "excess costs, expenses, and attorney fees reasonably incurred be-

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[9] In fact the district court's verbal admonishments to counsel may be viewed as sanctions. Only the most callous member of the bar would not feel the sting of the district court's order and take heed. Rule 11 gives a district court a broad range of sanctions from monetary fines to a "warm friendly discussion on the record". *See generally, Thomas v. Capital Security Services, Inc.*, No. 86-4480, —— F.2d ——, sl'p op. 1588) (5th Cir. January 21, 1988) (en banc) ("Whatever the ultimate sanction imposed the district court should utilize the sanction that furthers the purposes of Rule 11 and is the least severe sanction adequate to such purpose"). *Id.*

[10] 28 U.S.C. §1927 reads, in part: "*Counsel's liability for excess costs*: Any attorney . . . who so multiplies the proceedings in any case unreasonably and vexatiously may be required to satisfy personally the excess costs, expenses, and attorneys' fees reasonably incurred because of such conduct."

cause of such conduct." The language of the statute gives the trial judge express discretion whether to mete out sanctions, if a violation of §1927 is found. Because of its penal nature, §1927 has been strictly construed by the courts in reviewing cases in which sanctions are *granted*. *Indianapolis Colts v. Mayor and City Council*, 775 F.2d 177, 182 (7th Cir. 1985) (citing *Knorr Brake Corp. v. Harbil, Inc.*, 738 F.2d 223, 226 (7th Cir. 1984)). Accordingly, the courts have required a "clear showing of bad faith" in order for the penal sanctions of §1927 to attach. *Kamen v. American Tel. and Tel. Co.*, 791 F.2d 1006, 1010 (2d Cir. 1986) (citing *West Virginia v. Chas. Pfizer & Co.*, 444 F.2d 1079, 1082 (2d Cir. 1971), *cert. denied*, 404 U.S. 871 (1971)). Section 1927 has been reserved for the most egregious conduct.

The conduct adverted to in the Petition (at 5, 12) and in the district court's order (B-6) is generalized trial misconduct. While the court found the trial conduct "unprofessional", it did not find it conduct warranting a sanction. Without a trial transcript, Petitioner would have this Court second guess the discretion of the trial court and the court of appeals. The district court admonished Burulls' counsel for repeatedly attempting to elicit testimony ruled inadmissible and engaging in other conduct that unduly prolonged the trial, causing unnecessary delay, expense, and frustration. Beyond these generalized statements, there is no identification by the district court or by the petitioner of specific conduct warranting sanctions. The district court does not state or indicate that counsel's behavior was disrespectful, discourteous, or otherwise contemptuous. Petitioner has chosen not to provide a transcript of the trial proceedings and, accordingly, the district court's order finding this generalized misconduct not worthy of sanctions under §1927 is presumably correct. There

is simply no record on which to conclude that the district court abused its discretion in not meting out sanctions for trial misconduct.

Arthur Young also contends that it was an abuse of discretion in not meting out sanctions under §1927, after finding that the Burulls' claims were grounded on a false bankruptcy petition. The Burulls' claims were not grounded on a bankruptcy petition but on the wrongful conduct of Arthur Young and its codefendants. The bankruptcy petition is at most collateral to this proceeding.[11] "In any event, sanctions under §1927, unlike those under Rule 11, are discretionary, not mandatory." Court of Appeals, at A-5.

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[11] The bankruptcy petition contains a resolution stating that United States Satellite Services, Inc. is deadlocked; that the deadlock cannot be broken; that the resolution regarding the deadlock has been unanimously adopted by all shareholders entitled to vote. The district court found that "such resolutions in fact never existed and the evidence adduced at trial confirmed that Mr. Burull and his attorney knew such statements to be false." Petition, at B-4. The court did not find that the essence of the petition was incorrect. Apparently, no party objected to the filing of the resolution in Bankruptcy Court, which, as found by the court of appeals, has power to deal with such matters. Court of Appeals, at A-5, citing *Arkansas Communities, Inc. v. Mitchell*, 827 F.2d 1219 (8th Cir. 1987).

CONCLUSION

In summary, Petitioner asks this Court to consider questions of judicial discretion, which were carefully analyzed and correctly decided by the lower courts. Moreover, this Court is asked to review this case without benefit of a transcript. For the reasons stated above, the writ should be denied.

Respectfully submitted,

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